Higher Education Finance: Controlling Costs, Promoting Affordability and Developing a New Business Model

Natalie "Nikki" Krawitz
Higher Education Consultant

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Today's Session

- The challenges to the business model
- Public policy issues (e.g., cost, completion, and accountability) and the financial implications
- The responsibilities of Boards and their finance committees regarding higher education finance and financial oversight
- Institutional solutions to addressing the challenges

Challenges to the Business Model

- Tuition
  - Limited capacity for increases
  - Limited capacity for discounting
- Public funding
  - Decline
  - Competing needs
- Philanthropy
  - Unpredictable
  - Limited
- Investments
  - Volatility

Challenges to the Business Model

- Cross subsidies
- Educational Delivery
  - High school
  - On campus
  - Online
- Rising costs
  - Benefits
  - Technology
  - Utilities

Higher Education Issues & the Financial Impact

- Productivity & Efficiency
  - Administrative
  - Academic
- Access & Affordability
  - Student Aid
  - Educational Delivery
- Accountability
  - Quality
  - Completion

Changes in Student Attitudes & Goals: The Financial Implications

	1983	2013
Enrolled in top choice institution	73.7%	56.7%
Very important in deciding to go to this college		
Academic reputation	52.6%	64%
Received financial Assistance	20.8%	48.7%
Low cost/tuition	21.3%	45.9%
Concern about financing college		
None	33.5%	32.2%
Some	51.7%	55.1%
Major	14.9%	12.7%
Very good chance they will get a job to pay	36.6%	49.1%

Changes in Student Attitudes & Goals: The Financial Implications

	1983	2013
Very important reasons for going to college:		
To make more money	66.7%	73.3%
To be able to get a better job	76.2%	86.9%
Objectives considered to be very important		
Being very well off financially	69.3%	82%
Developing a meaningful philosophy of life	44.1%	44.8%

Best Practices for Ensuring Institutional Financial Sustainability:

Understanding how your institution is financially supported and capitalized

Board Financial Responsibilities

- Ensure that there is a clear definition of institutional mission and what that means
- Ensure that the budget is aligned with the institution's mission, strategic vision, goals, and priorities
- Ensure the institution is operating in a financially sustainable manner
- Ensure that resources are secured and appropriately allocated between long-term and short-term needs
- Ensure that resources are adequately protected, maintained, and renewed
- Ensure that all of those activities are accurately reported and understood by the board and the public
- Establish appropriate committees (Finance, Audit, Investments, Risk)
- Noses in; Fingers out

Understand how your institution is financially supported and capitalized

- Operating Statement – Statement of Revenues Expenses & Changes in Net Assets

- Balance sheet – Statement of Net Assets

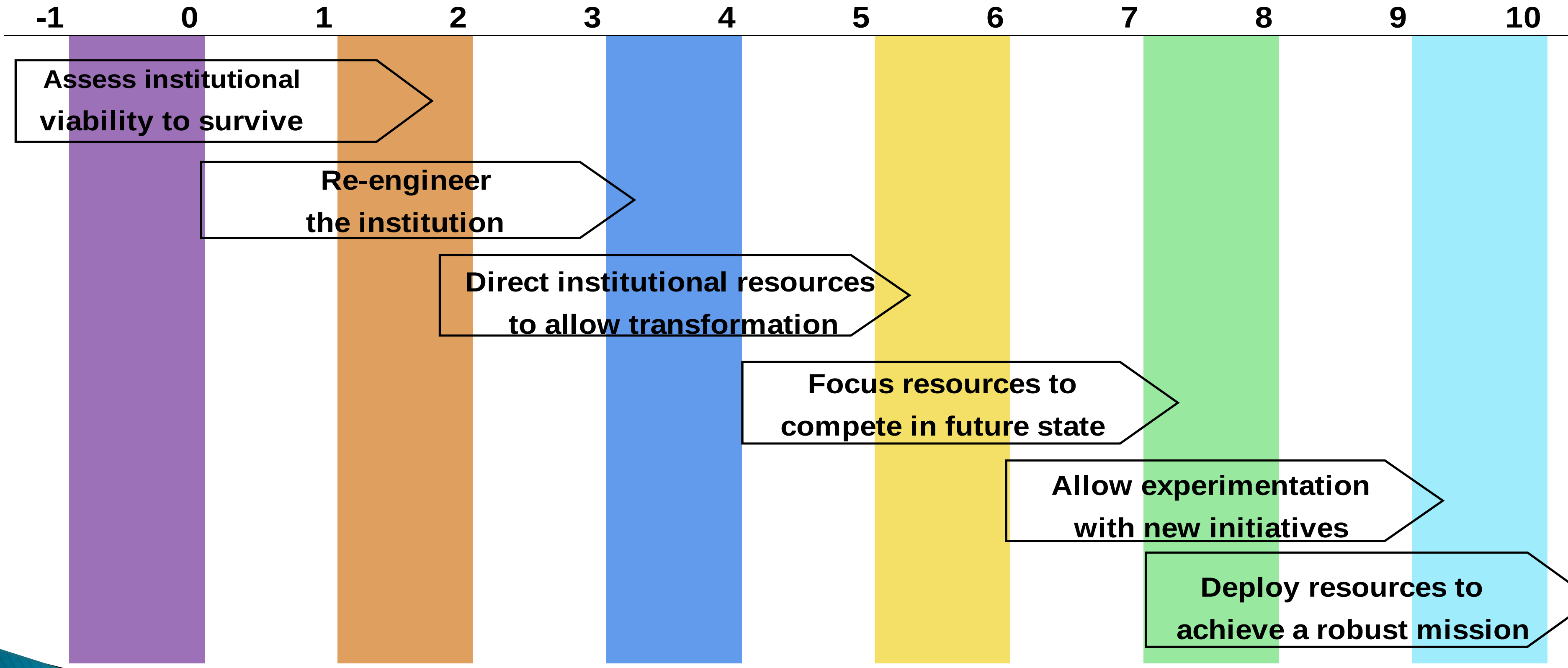
- Cash flows – Statement of Cash Flows.

Understand how your institution is financially supported and capitalized

- Use key performance metrics
  - Moody's and/or S&P Metrics
  - Trends over time
  - Performance compared to peers
  - Composite Financial Index:
    - Primary reserve ratio
    - Viability ratio
    - Net Income ratio
    - Return on Net Assets ratio

Example: Financial Strength Provides Flexibility to Make Strategic Investments

Scale for Charting Composite Financial Index Performance (3 year average)



Best Practices for Ensuring Institutional Financial Sustainability:

Understanding how your institution using is resources to achieve its mission and vision

Budgeting Best Practices

- Review and approve annual operating budgets
  - Oversee and challenge key budget & planning assumptions

  - Ensure that the budget is aligned with the strategic plan

- Ensure that annual operating budgets are in the context of long-range strategic financial planning

- Oversee and approve a long-term capital budget & review annually

Review and approve annual operating budgets

- **Key Operating Budget Questions**:
  - What are the key budget and planning assumptions for revenues and expenses? Are they realistic? What are the risks associated with each source?
  - What is the budgeted annual operating margin?
  - To what extent is reallocation built into the budget process?
  - Is the budget aligned with the strategic plan and mission?
  - Is resource investment tied to performance goals?
  - Is the budget consistent with long-term pricing strategy and goals for affordability?
  - How does the budget balance the need for investment in human and physical capital?
  - Does the budget reveal unmet needs and is it honest about the downside?

Elements of long-range strategic financial planning

- 3 to 5 year time-frame
- Scenario development
  - Optimistic
  - Base case
  - Pessimistic
- Revenue & expense assumptions
  - Financial objectives to reach budget equilibrium
    - Expenditure reductions to achieve budget equilibrium
    - Revenue generation to achieve budget equilibrium
  - Growth by substitution
- Sustainability of the business model: cost vs price
- Financial performance goals & metrics

Oversee and approve a long-term capital budget & review annually

- **Key capital budget questions**
  - Is there a long range capital plan?
  - What are the sources of funds for capital projects, how reliant is the institution on each & what are the key drivers and the risks?
  - What is the institution's policy for debt financing?
  - Has the institution explored partnerships with third parties to co-invest in new or renewed facilities?
  - What is the institution's approach to new facilities vs facility renewal and renovation?
  - Is it a net investor or net consumer of facilities assets? Renewal v Depreciation
  - Has the institution done a complete energy efficiency assessment?
  - Does budgeting for new facilities include provision for additions to the operating budget for ongoing utilities, maintenance and repair
  - Has the institution done a review of the condition of its facilities?
  - Does the institution use the FCNI (facilities condition needs index) to determine deferred maintenance and required investment?

5 Ways to Be More Cost Effective*

- Does our college or university pursue activities that are not critical to our mission?
- Are institutions operating at scale? Are facilities appropriately sized and used efficiently?
- Is the organizational structure efficient or does it lead to operational difficulties?
- Is the academic program efficient and does it optimize the use of faculty?
- Is our institution spending efficiently on financial aid?

*Lapovsky, Lucie, "5 Ways Your Institution Can Be More Cost Effective," Trusteeship, July/August 2012, V20, Number4.

Monitoring Budgets

- Ensure that operating & capital budgets are monitored on a continuous basis
  - Review quarterly budget to actual performance reports
    - Are actual results consistent with budget expectations?
    - What is the root cause of budget variances?
    - Is a budget variance the result of one-time or recurring transactions?
    - Does the budget need to be adjusted?
    - How do budgets and financial statements differ?
  - Regularly review progress on capital projects
  - Annually review debt financing and impact on financial statements

What Are Our Institutions Doing To Address the Challenges?

TRUMAN
STATE UNIVERSITY

Steps Taken to Deal with Financial Pressures

Dave Rector
Vice President for Finance & Administration

Steps Taken to Deal with Financial Pressures

- Lines of Business Analysis
  - Reviewed business support costs across all budget areas
  - Examples – photocopiers, phone lines, vehicles, printers
- Outsource vs Insource Review
  - Reviewed currently outsourced functions as well as potential for outsourcing
  - Examples – Information Technology, Printing Services, Recycling

TRUMAN STATE UNIVERSITY

Steps Taken to Deal with Financial Pressures

- Physical Plant Efficiencies
  - Cost benefit analysis led to replacement of central boiler system
  - Building utilization review – over 40,000 square feet eliminated to reduce overhead

- Key Question – what activities can we stop doing?

TRUMAN STATE UNIVERSITY

St. Louis Community College

Kent Kay
Vice Chancellor for Finance & Administration

Costs and Affordability

- Facilities and Technology
  - 54 buildings, 2.4M square feet, 391 acres, 10 locations
  - Previously set aside funding
  - Funding one-time purchases and projects from previous year's increase in net position
  - Reorganization of Technology to include better connectivity with functional personnel
    - Resultant reduction in administrative and supervisory positions
  - Flattened facility administration and management to improve service and reduce costs
    - One less administrator and three fewer managers

St. Louis Community College

Costs and Affordability

- Focus on Strategic
  - Student Experience
    - Act on consultant reports that call for reorganization of student services from a "one college" perspective
    - Efficiencies are expected throughout the upcoming year as action is implemented
  - Online Education
    - Leverage an investment from Technology Fee to expand services to online students and expand enrollment
  - Website redevelopment for better communication and service

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Costs and Affordability

- Programmatic Change
  - New programs developed with a business plan indicating sustainability
  - Generally requires "stopping something" in order to "start something"

St. Louis Community College

University of Missouri- Kansas City

- **Responsibility Center Management Philosophy**

- **Sharon Lindenbaum**
- **Vice Chancellor for Finance & Administration**

The Case for an RCM model

- Response to a changing environment
- Transparency
- Connection between performance and unit funding
- Authority and responsibility
- Spark for entrepreneurism and creativity

UMKC Model

- Net tuition
- State appropriations
- Special allocations
- Support costs
- Discretionary adjustments

Today

- Building a strong tie between student recruitment and retention efforts and the allocation of general revenue

- Changing the conversation on campus around budgeting

- Bringing new focus to fiscal accountability and responsibility

- It is a journey, not a destination.

Questions?